



Auditor-General of South Africa

# Big 5 Hlabisa Municipality - audit report 2016-17

# Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Big 5 Hlabisa Municipality

## Report on the audit of the financial statements

### Opinion

1. I have audited the financial statements of the Big 5 Hlabisa municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Big 5 Hlabisa municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

### Basis for opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### Material uncertainty relating to going concern

6. As disclosed in note 44 to the financial statements the municipality has unspent conditional grants that are not cash backed and the municipality's current liabilities exceeded its total assets by R16,92 million. These conditions, along with other matters as set forth in note 44 to the financial statements, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern. Management plans to improve financial sustainability by implementing cost containment measures in conjunction with revenue enhancement strategies.

### Emphasis of matter

7. I draw attention to the matter below. My opinion is not modified in respect of this matter.

## Irregular expenditure

8. Note 32 to the financial statements indicates that the municipality has incurred irregular expenditure to the amount of R70,25 million, as proper supply chain management processes had not been followed.

## Other matter

9. I draw attention to the matter below. My opinion is not modified in respect of this matter.

## Unaudited disclosure notes

10. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

## Responsibilities of the accounting officer for the financial statements

11. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA, DoRA and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
12. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to liquidate the municipality or cease operations, or there is no realistic alternative but to do so.

## Auditor-general's responsibilities for the audit of the financial statements

13. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
14. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.



## **Introduction and scope**

15. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
16. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
17. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2017:

<b>Development priorities</b>	<b>Pages in the annual performance report</b>
Local Economic Development	10
Basic service delivery	11 – 13

18. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
19. The material findings in respect of the usefulness and reliability of the local economic development priority is as follows:

### **Local economic development**

#### **Upgrade and formalize informal trading zone in two wards by 30 June 2017 – not well defined and reliable**

20. The source information and evidence for the achievement of the planned indicator was not clearly defined, as required by the Framework for Managing Programme Performance Information (FMPPI).
21. The reported achievement for the indicator was misstated as the evidence provided indicated 1 and not 2 as reported.

### **Promote government LED programmes iro. EPWP – not reliable**

22. The reported achievement for the indicator was misstated as the evidence provided indicated 83 and not 143 as reported.

### **Number of co-operatives established and registered – not reliable**

23. The reported achievement for the indicator was misstated as the evidence provided indicated 6 and not 11 as reported.

24. I did not identify any material findings on the usefulness and reliability of the reported performance information for the basic service delivery development priority.

### **Other matters**

25. I draw attention to the matters below.

### **Achievement of planned targets**

26. The annual performance report on pages x to x and x to x includes information on the achievement of planned targets for the year and explanations are also provided for the under and overachievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 20 to 23 of this report.

### **Adjustment of material misstatements**

27. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of local economic development and basic service delivery development priorities. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information for local economic development.

## **Report on the audit of compliance with legislation**

### **Introduction and scope**

28. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

29. The material findings on compliance with specific matters in key legislation are as follows:

### **Annual financial statements**

30. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets and disclosure items identified by the auditors in the

submitted financial statements were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

### **Strategic planning and performance management**

31. The performance management system and related controls were not maintained as it did not describe how the performance review and reporting processes should be conducted, organised and managed, as required by section 7(1) of the Municipal Planning and Performance Management Regulation, 2001.

### **Budgets**

32. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R11,49 million, as disclosed in note 33 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by overspending on employee costs and general expenditure.

### **Procurement and contract management**

33. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of Municipal Supply Chain Management Regulation, 2005 (MSCMR) 17(a) and (c).
34. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by MSCMR 19(a).
35. Quotations and contracts were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by MSCMR 13(c). Similar non-compliance was also reported in the prior year.
36. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act No. 5 of 2000).
37. Bid documentation for procurement of commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by Preferential Procurement Regulation of South Africa, 2011, 9(1).
38. Sufficient appropriate audit evidence could not be obtained that all extensions or modifications to contracts were approved by a properly delegated official, as required by MSCMR 5.
39. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. This non-compliance was identified in the procurement processes for the Gabadela and Mavema electrification project and the Iseluleko project.



40. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, in contravention of section 116(2)(c) of the MFMA.

### **Human resource management**

41. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).

### **Expenditure management**

42. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
43. Effective steps were not taken to prevent irregular expenditure amounting to R70,25 million as disclosed in note 32 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with the MSCMR.
44. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R356 990, as disclosed in note 31 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalties as a result of late payments of suppliers and SARS.

### **Consequence management**

45. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) and (b) of the MFMA.

<b>Other information</b>
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46. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the foreword by the mayor, foreword by the municipal manager and the audit committee's report. The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in the auditor's report.
47. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
48. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

49. The other information I obtained prior to the date of this auditor's report is the foreword by the mayor and the foreword by the municipal manager. The audit committee's report is expected to be made available to me after 30 November 2017.
50. If, based on the work performed on the foreword by the mayor and the municipal manager, that I obtained prior to the date of this auditor's report, I conclude that there is a material misstatement, I am required to report that fact. I have nothing to report in this regard.
51. When I do receive and read the audit committee report, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate, however, if it is corrected this will not be necessary.

#### **Internal control deficiencies**

52. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon.
53. The matters reported below are limited to the significant internal control deficiencies that resulted the findings on the annual performance report and the findings on compliance with legislation included in this report.

#### **Leadership**

54. The accounting officer did not exercise adequate oversight responsibility regarding performance reporting and compliance with legislation. In this regard, the accounting officer did not ensure the policies and procedures are appropriately implemented to support the achievement of credible reporting and compliance with legislative requirements.

#### **Financial and performance management**

55. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information as evidenced by the material misstatements identified in the annual financial statements and material findings on the annual performance report. This was due to management not fully understanding the requirements of the financial and performance reporting frameworks and vacancies in key management positions.

*Auditor-General*

Pietermaritzburg

30 November 2017





AUDITOR-GENERAL  
SOUTH AFRICA

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## **Annexure – auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality’s compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in the auditor’s report, I also:
  - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control.
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
  - conclude on the appropriateness of the accounting officers’ use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Big 5 Hlabisa municipality ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause a municipality to cease continuing as a going concern.
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.



